The AAII Journal

American Association of Individual Investors

2007 Personal Tax & Financial Planning Guide

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Introduction

Our 2007 Personal Tax and Financial Planning Guide is designed to help you assess your current tax situation and plan for any changes that may improve your tax liability both this year and next.

This year's Guide includes:

- A review of tax changes that may affect your situation for this year and beyond;
- A review of planning strategies you should consider, including the timing of income and deductions;
- A review of the tax rules and other considerations for the most common personal investments; and
- Helpful worksheets and summaries for reviewing your current tax position and for further tax planning, including a summary of the tax rate schedules, deductions, exemptions, phase-outs, and other helpful tax numbers for tax years 2007 and 2008; a Tax Forecasting Worksheet; and a Yearly Tax Planning Calendar.

We hope you find this Guide useful, but every individual's circumstances differ, and we encourage you to consult with your tax advisor where specific advice is appropriate.

Maria Crawford Scott
Editor, AAII Journal

Personal Tax Planning 2007

Tax Changes: 2007 Legislation

As of this writing in mid-November, taxpayers have not yet received any last-minute relief from the alternative minimum tax (AMT). Barring relief, the exemption amount for 2007 will drop to $45,000 (down from $62,550) for married taxpayers filing jointly, and to $33,750 (down from $42,500) for single taxpayers.

Although many expect that some form of relief will be granted for the 2007 tax year, without further action by Congress, the AMT exemption amount decrease could subject many millions of taxpayers to the AMT.

To date, Congress has passed little tax legislation in 2007 that affects individual taxpayers. One area of change, however, is the "kiddie tax." The Small Business and Work Opportunity Tax Act of 2007 raised the age at which children with unearned income above a minimum amount are taxed at the parent's rate. In 2007, the kiddie tax age remains at 18, but beginning in 2008 the age can range from 19 to 23, depending on whether they are dependents and/or full-time students.

Prior legislation has left a complicated array of changing tax rates and benefit phaseout levels—all of which will expire in 2010. Congress is sure to change this, but that leaves taxpayers with considerable uncertainty even before 2010, which makes planning difficult.

Known Tax Law Changes

The Tax Relief Extension Reconciliation Act of 2005, signed into law in 2006, extended through December 31, 2010, the dividend and capital gains tax cuts that were enacted in 2003 and scheduled to expire at the end of 2008.That means that, through 2010, the maximum tax rate for capital gains and qualified dividends is 15%; taxpayers in the 10% and 15% tax brackets benefit from an even lower maximum rate of 5%, and that drops to 0% in 2008.

The extensions provided in the 2005 Tax Reconciliation Act mean that the dividend and capital gains tax cuts expire at the same time as the tax cuts that were passed by the Economic Growth and Tax Relief Reconciliation Act of 2001 and extended by the Working Families Tax Relief Act of 2004. Those tax cuts included lower marginal income tax rates, relief from the marriage penalty and temporary repeal of the federal estate tax.

Individuals with substantial investment income can continue to see significant tax savings this year as well as over the next several years, if they take advantage of the planning opportunities. However, in considering any investment strategy, you should keep in mind that most of the provisions are still only temporary. After 2010, tax rates are set to revert to earlier levels, with a 39.6% top marginal income tax rate, a 20% top capital gains rate and dividends taxed as ordinary income. In addition, the estate tax and gift tax rates revert to pre-2001 levels.

The provisions of the 2005 Tax Reconciliation Act, and the 2004 Tax Relief Act combined with the provisions of the 2001 and 2003 Tax Acts, are presented in summary form in Table 1.

What's New for 2007

Listed below are tax change highlights for 2007, tax changes that are currently set to go into effect in 2008, as well as some old rules you may want to keep in mind when going through your year-end review.

Alternative Minimum Tax

As of this writing, Congress was considering extending the 2006 alternative minimum tax (AMT) exemption amount at least through 2007. However, under current law, the 2007 exemption amount is set to decrease to $45,000 for married filing joint taxpayers, and to $33,750 for single and head of household taxpayers, which could push many middle-income families into the alternative minimum tax. The 2006 AMT exemption amounts were $62,550 for married filing joint taxpayers, and $42,500 for

single and head of household taxpayers.

Standard Deduction

For 2007, the standard deduction increases to $10,700 for married couples filing a joint return, $5,350 for singles and $7,850 for heads of household.

In 2008, that amount increases to $10,900 for married couples filing a joint return, $5,450 for singles and $8,000 for heads of household.

Personal Exemptions

For 2007, the personal exemption amount increases to $3,400; in 2008, that amount increases to $3,500.

Taxpayers with adjusted gross incomes above a certain amount may lose part of the benefit of the exemption, but the amount by which these benefits are reduced in 2007 is only two-thirds of the reduction that would have applied otherwise.

In 2007, the adjusted gross income amounts at which phase-outs begin increase to $234,600 for married persons filing jointly, $156,400 for singles and $195,500 for heads of household.

Individual Retirement Accounts and 401(k) Plans

In 2007, the maximum annual contribution for IRAs remains at $4,000 (although it increases to $5,000 for any individual who is age 50 or older); in 2008, the maximum annual contribution for IRAs increases to $5,000 ($6,000 for any individual who is age 50 or older).

In 2007, the maximum annual contribution limit for 401(k)s increases to $15,500 ($20,500 if you are age 50 or over); in 2008, those limits will remain at the 2007 level. For SIMPLE plans, the maximum annual contribution is $10,500 ($13,000 for those age 50 or over); those limits will remain the same in 2008.

Qualified Plan Contributions

In 2007, the maximum annual contribution for qualified plans, including SEP and Keogh plans, increases to $45,000; in 2008, that amount will increase to $46,000.

Estate and Gift Tax Limits

In 2007, the estate tax exemption remains at $2 million and the annual gift exclusion remains at $12,000. Those levels remain unchanged in 2008.

Child Tax Credit

The child tax credit for dependent children younger than 17 remains at $1,000 through 2010.

Kiddie Tax

In 2007, the "kiddie tax" applies to children up to age 18, and starting in 2008, it could apply to children up to age 24, depending on how much earned income they have and whether or not they are full-time students.

Under the kiddie tax rules, children with investment income above a certain amount may have part or all of their investment income taxed at the parents' income tax rate. For 2007, the kiddie tax rule applies if the child is 17 or under by the end of the year, and the child's total investment income for the year was more than $1,700.

Starting in 2008, new rules extend the kiddie tax to older children, depending on how much earned income they have and whether or not they are full-time students:

- Starting in the year that your child turns 18, the kiddie tax will apply if your child's earned income (including salaries and wages, commissions, professional fees and tips) is less than half of the child's overall support.
- Starting in the year your child turns 19, the kiddie tax will apply if your child is a full-time student.
- The kiddie tax will stop applying in the year your child turns 24.
- The kiddie tax will also not apply if your child is married filing jointly.

Charitable Donations

Last year, the rules for certain charitable contributions tightened.

Beginning with contributions made after August 17, 2006, no deduction is allowed for most contributions of clothing and household items unless the donated property is in good used condition or better.

In 2007, charitable contributions of cash (regardless of the amount) to any qualified charity must be supported by a dated bank record (such as a cancelled check) or a dated receipt from the charity that must include the name of the charity, date and the amount of the contribution.

Medicare Part D

Taxpayers who itemize deductions can deduct (as a medical expense) the premiums they pay for the new Medicare Part D prescription drug insurance program.

Sales Tax Deduction

Last year, Congress extended the provision allowing taxpayers who itemize deductions the option of choosing between a deduction of sales taxes or income taxes when claiming a state and local tax deduction, but this option expires after 2007.

Itemized Deduction Phase-Outs

Taxpayers with adjusted gross income above a certain amount may lose part of the benefit of their itemized deductions, but the amount by which these benefits are reduced in 2007 is only two-thirds of the reduction that would have applied otherwise.

In 2007, the adjusted gross income amounts at which phase-outs begin increase to $156,400 for married persons filing jointly, singles and heads of household.

Taxwise

Planning Considerations: Married filing joint taxpayers will need to calculate whether taking the increased standard deduction or itemizing deductions will generate the most tax savings overall. In doing so, make sure to consider whether state law restricts the ability to itemize to only those who itemize for federal purposes. The higher deductions may also require more couples to pay alternative minimum tax (AMT).

Taxable Income Limits for 1040A and 1040EZ

The income limit for using Form 1040A and Form 1040EZ in 2007 is taxable income of less than $100,000, assuming you meet all of the other requirements for using those forms.

Tax-Exempt Interest Reporting

Beginning last year, state and local governments are required to report interest paid on tax-exempt state and local bonds on Form 1099-INT, Interest Income. This amount must be shown on your tax return and is for information only.

Health Savings Accounts

You may be able to take a deduction if you contributed to a Health Savings Account (see box below).

HEALTH SAVINGS ACCOUNTS

You may be able to deduct contributions to a Health Savings Account (HSA). These tax-free savings accounts were established under the Medicare Act of 2003, and can be used to pay for medical expenses incurred by you, your spouse or dependents. They are used in conjunction with high-deductible health plans, where your basic health insurance does not cover first-dollar medical expenses.

HSAs may be established by anyone who is covered by an HSA-qualified "high-deductible health plan," is not covered by any other health insurance and is not enrolled in Medicare. Qualified high-deductible health plans must have an annual deductible of at least $1,100 for individuals and $2,200 for families in 2007; these minimum deductibles will remain at those levels in 2008.

Tax-deductible contributions can be made into the health savings account for the full amount of the annual deductible each year, up to a maximum of $2,850 for individuals and $5,650 for families in 2007. These amounts are increased annually for inflation; in 2008, they will increase to $2,900 for individuals and $5,800 for families. If you are over age 55, you can make extra contributions to your account ($800 in 2007, increasing to $900 in 2008 and $1,000 in 2009 and thereafter) and still enjoy the same tax advantages.

And, beginning in 2007, individuals can make a one-time transfer from their IRA to an HSA, subject to the contribution limits applicable for the year of the transfer.

Contributions to HSAs can be made by you, your employer, or both. You can fully deduct your own contributions to an HSA, even if you do not itemize, and contributions made by your employer are not included in your taxable income. The interest and investment earnings generated by the account are also not taxable while in the HSA.

Amounts distributed from the HSA are not taxable as long as they are used to pay for qualified medical expenses. They can be used to:

- *Cover the health insurance deductible and any co-payments for medical services, prescriptions, or products;*
- *Purchase over-the-counter drugs and long-term care insurance and expenses; and*
- *Pay health insurance premiums or medical expenses during any period of unemployment.*

Amounts distributed that are not used to pay for qualified medical expenses will be taxable, plus a 10% penalty will be applied.

HSAs are similar to IRAs in that they are owned by individuals – you are not dependent on a particular employer to enjoy the advantages of an HSA. And if you change jobs, the HSA goes with you.

What if you already have an existing medical savings account (MSA)? In that case, you can either retain it or roll the amount over into a new HSA.

For more information on HSAs, go to the U.S. Treasury's Web site at www.treas.gov and click on Health Savings Accounts.

Table 1. An Overview of Tax Changes in the Coming Years

	2007	2008	2009	2010	2011
Long-Term Capital Gains Rate					
Tax Bracket Above 15%	15%	15%	15%	15%	20%
Tax Bracket 15% or Below	5%	0%	0%	0%	10%
Qualified Dividends Rate					
Tax Bracket Above 15%	15%	15%	15%	15%	na*
Tax Bracket 15% or Below	5%	0%	0%	0%	na*
Marginal Income Tax Rates					
Top Bracket	35%	35%	35%	35%	39.6%
Fifth Bracket	33%	33%	33%	33%	36%
Fourth Bracket	28%	28%	28%	28%	31%
Third Bracket	25%	25%	25%	25%	28%
Second Bracket	15%	15%	15%	15%	15%
First Bracket	10%	10%	10%	10%	na
Child Tax Credit	$1,000	$1,000	$1,000	$1,000	$500
Marriage Penalty Relief					
Standard Deduction (% of S.D. for singles)	200%	200%	200%	200%	na
15% Tax Bracket (% of bracket for singles)	200%	200%	200%	200%	na
Repeal (%) of Personal Exemptions Phase-outs	33.3%	66.6%	66.6%	100%	na
Repeal (%) of Limitation on Itemized Deductions	33.3%	66.6%	66.6%	100%	na
AMT Exemption					
Single	$33,750*	$33,750	$33,750	$33,750	$33,750
Married Filing Joint	$45,000*	$45,000	$45,000	$45,000	$45,000
Head of Household	$33,750*	$33,750	$33,750	$33,750	$33,750
Estate Tax					
Exclusion	$2 million	$2 million	$3.5 million	Tax repealed	$1 million
Maximum Rate	45%	45%	45%	0%	55%

*Qualified Dividends: * Taxed as ordinary income.*

*AMT Exemption: * As of 11/15/07. However, Congress is considering legislation that may raise those levels for 2007.*

Education Savings

You can make non-deductible contributions to qualified tuition plans, also known as section 529 plans. These accounts, offered by states or their designee, are maintained solely for the qualified higher education expenses of a beneficiary. Distributions are tax-free, provided that the distributions are used to pay qualified expenses.

In 2007, the contribution limit for an education IRA, now known as a Coverdell Education Savings Account, remains at $2,000 per beneficiary. The contributions are not deductible, but they grow tax-free in the IRA. Coverdell accounts may be used to fund qualified elementary, secondary, and higher education expenses. However, the amount that can be contributed is limited for higher-income taxpayers.

Investment Strategies: 2007 and Beyond

Given the nature of the tax cuts and changes in the past few years, tax planning opportunities also give rise to investment planning opportunities. However, your

goals and risk tolerance should drive your investment decisions, not just the income tax impact of an investment.

Take Advantage of Lower Marginal Rates

Under the pre-2003 tax rate structure, deferring income that was taxed at higher ordinary tax rates made sense, but now qualified dividends and long-term capital gains are taxed at the same rate, and in 2008 the rates are set to decline to 0% for taxpayers in the 15% or below tax brackets. However, these rates will expire at the end of 2010, and the outlook for extending these advantageous rates beyond 2010 is uncertain at best.

In terms of tax strategies, we suggest you consider maintaining a balanced exposure to both value and growth strategies.

Sell Low-Basis Stock

The current tax environment continues to present the perfect opportunity to sell low-basis stock held for more than one year, because long-term capital gains rates may never be lower. Indeed, capital gains rates will revert to previous higher levels starting in 2011. If you have large positions in either gifted or inherited stocks, or stocks received from a sale of a business, consider using the proceeds from selling the stock to diversify your portfolio.

Consider the Impact of Taxes on Mutual Fund Investments

Selecting tax-aware managers of mutual funds may be important to maximizing your aftertax rate of return in your taxable (i.e., not a retirement account) investment portfolio. You may choose when to sell shares of the fund and may, therefore, create long-term versus short-term capital gains. But you don't control the investments within the fund. Should an equity manager fail to extend the holding period on a stock, it could cost you 20% of your gain (35% ordinary rate for short-term capital gains versus 15% long-term capital gains rate).

Some mutual fund dividends will qualify for the 15% rate, while others will not. Dividends paid by stocks held by the fund and passed through to the shareholder will qualify for the dividend tax rate. However, capital distributions and bond interest will not. These payments are reported to the IRS on Form 1099, which specifies the type of distribution.

Reconsider Taxable vs. Tax-Free Bonds

Due to reduced tax rates, the aftertax yield on taxable bond investments has increased for certain taxpayers. Therefore, investments in tax-free bonds may be less attractive. Additionally, private-activity bonds (a type of tax-free bond) could increase your exposure to the alternative minimum tax since their interest income is taxable for purposes of the alternative minimum tax. You should review your bond and money market accounts to make sure that you are earning the highest aftertax return. Don't forget to consider the state tax implications of switching from tax-free to taxable bonds before making any final portfolio decisions.

Consider Increasing Retirement Savings

You may want to use any additional cash flows you receive this year to increase the amount invested in an IRA or 401(k) plan. The main advantage of retirement accounts—tax deferral—continues to make them a good investment vehicle.

Review the Tax Implications of Taxable vs. Tax-Deferred Accounts

The spread between capital gains and ordinary income rates has important implications regarding your asset allocation between taxable and tax-deferred (retirement) accounts. For example, from a tax perspective holding individual stocks in tax-deferred accounts and bonds in taxable accounts could be expensive, because gains resulting from stocks held in tax-deferred plans such as IRAs or 401(k) plans will be taxed at ordinary rates when taken as a distribution. By reversing that structure, taxable bonds and other tax-inefficient assets will be shielded from tax in the deferred accounts while equities will enjoy the reduced rates for dividends and capital gains in personal accounts. Tax-free municipal bonds should, of course, remain outside of retirement accounts. Individuals should also consider the cost of commissions and taxes, as well as current cash flow needs, before making any investment moves between taxable and tax-deferred accounts.

Protect Social Security Benefits

If you are receiving Social Security benefits, you may have to pay taxes on them if your "modified" adjusted gross income (primarily your taxable income plus any tax-exempt interest income plus half of your Social Security benefits) exceeds certain levels. To protect your benefits, watch the amount of interest you receive from municipal bonds, since this amount is included in your modified adjusted gross income when determining the Social Security benefit taxability. In addition, you may want to delay taxable distributions from a retirement plan or IRA to the extent you are able.

Conclusion

It is important to remember that taxes are not the key to investment planning. And the temporary duration of many of the current tax law provisions should motivate individuals to reconsider existing strategies in the com-

ing years.

However, one thing is certain: There will be more tax changes coming. Congress will be addressing these tax issues again as the expiration dates of the lower tax rates near. Although many taxpayers can expect tax savings in the near future—especially high-wealth individuals with substantial investment income—everyone should consider how the changes directly affect their overall tax and investment strategies.

Year-End Tax Planning

All Taxpayers: Determine Where You Are Now

Year-end planning gives you the opportunity to shift certain items around, should that be beneficial in terms of your tax liability. Taking a few initial steps now and using year-end planning strategies can result in significant tax savings.

How can you effectively plan?

Here are the basic steps you should take to help start your personal tax planning:

- First, estimate your income, deductions, credits, and exemptions for 2007 and 2008 using the Tax Forecasting Worksheet (page 23);
- Identify items that you can shift from 2007 into 2008 and beyond (or vice versa);
- Determine your marginal tax rate—the rate at which your next dollar of income will be taxed—for 2007 and 2008;
- Determine how much tax you owe and when you must pay it to avoid underpayment penalties;
- Determine whether you are subject to the alternative minimum tax (AMT);
- Consult with your tax advisor, and then take the actions needed to make the best of your tax situation.

To minimize your taxes, consider both short-term and long-term tax planning issues and strategies. Starting early will give you extra time to obtain additional information about items that concern you and to investigate additional ideas for tax savings or deferral. The Tax Forecasting Worksheet on page 23 will help you to view the current year and next year together and will provide a starting point for evaluating the tax effects of various strategies.

Avoiding Tax Underpayment Penalties

Make sure you determine your 2007 tax liability and the due dates for paying those taxes (including self-employment tax and the alternative minimum tax [AMT]), so that you avoid underpayment penalties.

Federal tax law requires the payment of income taxes throughout the year as you earn your income. This obligation may be met through either withholding, quarterly estimated tax payments, or both. If you do not meet this obligation, you may be assessed an underpayment penalty.

For 2007, if your total tax due minus the amount you had withheld is less than 10% of your total tax due, you will not be assessed an underpayment penalty. The disadvantage of overpaying throughout the year, though, is that you are in effect making an interest-free loan to the government. However, the underpayment penalty can be high, and it is calculated as interest on the underpaid balance until it is paid, or until April 15, 2008, whichever is earlier.

You can avoid underpayment tax penalties by adopting one of the safe harbor rules. The basic rule is to pay the required amount by the end of the year through withholding and quarterly estimated payments. The required amount will be one of the following, depending on your individual situation:

- 90% of the current year's tax liability;
- 100% of the prior year's tax liability (increases to 110% for taxpayers who had adjusted gross income in excess of $150,000 in 2006); or
- 90% of the tax liability based on a quarterly annualization of current year-to-date income.

Penalties are based on any underpayment, which is the difference between the lowest amount required to be paid by each quarterly payment date and the amount actually paid by that date. The annual required amount, based on either of the first two alternatives, is paid in equal installments. In the case of the third method, which is based on annualized income, the amount due each quarter is based on actual income received for each installment period. The third method is typically more beneficial if you expect to receive most of your income during the latter part of the year. It allows for lower required payments in the early quarters.

Payments made through with-

How Much of Your Social Security Is Taxed?

Income Level	Percent of SS Benefits Taxed
Below $25,000 Single & Head of Household Below $32,000 Married Filing Jointly	0%
$25,000 to $34,000 Single & Head of Household $32,000 to $44,000 Married Filing Jointly	50%
Above $34,000 Single & Head of Household Above $44,000 Married Filing Jointly	85%

holding from your paycheck (or from your pension or other payments) are given special treatment. The IRS treats income tax that is withheld as having been paid equally throughout the year (unless you prefer to use actual payment dates). This lets you make up for underpaid amounts retroactively, because amounts withheld late in the year may be used to increase the amounts paid in earlier quarters.

Taxwise

State and Local Rules: Be aware that many states have underpayment rules that vary from the federal requirements.

Timing: Income & Deductions for Taxpayers Not Subject to AMT

You have opportunities to reduce your taxes if you can control the timing of either your income or expenses. However, it is important to make sure you understand whether you may be subject to the alternative minimum tax (AMT) before adopting these strategies (see box below).

Income

Your income is generally taxed in the year of receipt, so having the ability to control when you receive it affords a strategic tax planning opportunity. Deferring income until a later year will, in most cases, delay the payment of tax. You cannot defer taxation by merely delaying receipt of the income if the funds are available to you and the time of payment is subject to your unrestricted discretion. Any decision to defer income must be weighed with the lost time-value of the money and other risks that could alter or forfeit your right to the income.

The timing of bonuses, recognition of capital gains from the sale of stocks, and the exercise of non-qualified stock options are all events that can easily be delayed into a subsequent year. You should also consider the deferral of compensation through the use of various retirement plans and deferred-compensation arrangements. If you operate a business or collect rental income and report that income on the cash receipts and disbursements method, you have an opportunity to delay or accelerate the billing to your customers or tenants and determine the timing of the related income.

While most taxpayers are better off deferring income and thus deferring taxes, some individuals may actually want to consider accelerating income into 2007 due

AMT: AN UNPLEASANT SURPRISE

Are you subject to the alternative minimum tax? This tax comes as a surprise to many taxpayers. You may be subject to this tax, especially if any of the following criteria apply to your situation:

- *You have large itemized deductions for state and local taxes, including property and state income tax, or from state sales tax;*
- *You have exercised incentive stock options;*
- *You have significant deductions for accelerated depreciation;*
- *You have large miscellaneous itemized deductions; and*
- *You have tax-exempt income from private-activity bonds.*

The alternative minimum tax is calculated by first determining the tentative minimum tax. The tentative minimum tax is 26% of the first $175,000 ($87,500 married filing seperately) of alternative minimum taxable income in excess of the exemption amount, plus 28% of any additional alternative minimum taxable income. However, for alternative minimum tax purposes, dividends and capital gains will be taxed under the same rules as for regular tax calculations. The alternative minimum tax is the excess of the tentative minimum tax above the regular tax calculated.

Alternative minimum taxable income adds back certain preference items to regular taxable income, including state income taxes, real estate taxes and miscellaneous itemized deductions, and can cause the alternative minimum tax to be larger than the regular tax.

In addition, although the tax rate on capital gains and dividend income is the same for both regular tax and alternative minimum tax, the disparity in rates between the alternative minimum tax and the regular tax may result in a higher effective rate on all income, including capital gains and dividends.

Taxwise

The IRS offers the AMT Assistant, an electronic version of the AMT Worksheet in the 1040 Instructions. By filling in a few simple questions, you can determine whether or not you owe the alternative minimum tax. Go to the AMT Assistant at www.irs.gov (found in the Online Tools section).

to the unusual nature of the tax rates over the next few years. For example, individuals in the 15% and below tax bracket may want to take advantage of the 0% capital gains rate starting in 2008. Accelerating income into 2007 may assure they qualify for the 0% rate in 2008.

Deductions

You can reduce taxes by controlling the payment of deductible expenses. If paid by December 31, you may deduct certain expenses that are due next year on your 2007 return. This strategy helps most when you expect this year's marginal tax rate to be higher than next year's. Taking the deduction in a year with a higher rate makes the deduction worth more. Again, you must balance this decision with the time-value of money and other inherent risks.

For example, if you pay a deductible expense in December 2007 instead of April 2008, you reduce your 2007 tax instead of your 2008 tax, but you also lose the use of your money for three-and-one-half months. Generally, this will be to your advantage, unless you have an alternative use for the funds that will produce a very high return in that three- or four-month period. You must decide whether the cash used to pay the expense early should be used for something more urgent or more valuable than the accelerated tax benefit.

Another consideration concerning the timing of deductions is that for higher-income taxpayers, the "phaseout" on itemized deductions is reduced in 2008. That means that for these taxpayers, in 2008 less of their income will be taxed and their deductions will count for more.

For those who will pay 2008 estimated taxes based on their 2007 tax liability, reducing your 2007 taxes has another advantage: Your 2008 estimated tax payments may be smaller.

State Taxes

If accelerating deductions makes sense for you and you choose to claim a deduction on your state and local income taxes, you may want to prepay the balance on your estimated state tax liability in December, rather than waiting until 2008. This secures that deduction on your 2007 tax return, even though the payment might not be required by the state until January 15, 2008, or April 15, 2008.

Charitable Contributions

If you are planning on making a gift to a charity in 2008, consider making the gift in 2007 to accelerate the tax benefit of the contribution. However, it is important to note that certain limitations exist with respect to deductions for charitable contributions.

You should also consider the benefits of gifting appreciated stock to a charity. If you donate long-term appreciated stock directly to the charity, you get a deduction for the full fair market value of the stock; whereas if you sell the stock first and donate cash, you only get a deduction for the aftertax cash donated.

When making a gift to charity, you must have an appropriate record of the gift in order to properly support the deduction. Starting in 2007, cash contributions of any amount must be supported by a written record either in the form of a bank record (for example, a cancelled check) or a written receipt from the charity. The record must include the name of the charity, the date, and the amount of the contribution.

Prepaid Interest

A cash basis taxpayer may not deduct prepaid interest before the tax year to which the interest relates. However, there is some flexibility to prepay year-end interest that is due early in the following year. For example, if a mortgage payment is due on January 10, a taxpayer can accelerate the deduction of the portion of the interest relating to the period up to January 1 by mailing the check in December.

The most significant interest deductions currently available are for home mortgage interest and for investment

WHERE'S MY MONEY? TRACKING YOUR REFUND 24/7

If you are expecting a refund on your 2007 income tax, you can check on its status if it has been at least six weeks from the date you filed your return by mail, or three weeks if you filed electronically. You will need to supply the following information: your Social Security Number or IRS Individual Taxpayer Identification number, your filing status, and the exact whole-dollar refund amount as it is shown on your return. You can check the status of your refund in two ways:

- *On the Internet, go to www.irs.gov and click on "Individuals" and then "Where's My Refund?"*
- *By telephone (for automated information), call 800/829-4477.*

If you are unable to get information on your refund through either of these two automated services, you can call the IRS for assistance at 800/829-1954.

The site also allows you to start a trace for lost or missing refund checks, or to notify the IRS of an address change when refund checks go undelivered. Taxpayers can avoid undelivered refund checks by having refunds deposited directly into a personal checking or savings account. This option is available for both paper and electronically filed returns.

interest expense to the extent of current-year investment income. Interest paid in relation to investments that earn a tax-free return is not deductible.

Medical Expenses

If the timing of certain medical and dental expenditures is flexible and your overall medical expenses are high in the current year, you may want to accelerate payment of these expenses. Because unreimbursed medical expenses are only deductible to the extent that they exceed 7.5% of adjusted gross income, it is best from a tax standpoint to incur expenses—such as replacement eyeglasses or contact lenses, elective surgery, dental work, and routine physical examinations—in a year in which you have already gone over (or the added expenses would take you over) the 7.5% threshold.

Miscellaneous Itemized Deductions

Miscellaneous itemized deductions are only deductible to the extent that they exceed 2% of adjusted gross income. This category is large but includes:

- Tax preparation fees such as tax preparation software, tax publications and any fee paid for electronic filing; and
- Investment fees, custodial fees, trust administration fees, and other expenses paid for managing your investments that produce taxable income.

Accelerating miscellaneous itemized deductions only benefits taxpayers who accumulate expenses sufficient enough to exceed the 2% threshold. If possible, it may be advantageous to pay these types of expenses in one year if, because of the 2% floor, you would not receive a benefit of the deduction in each of the two consecutive years.

Timing Caution for Taxpayers Subject to AMT

The alternative minimum tax (AMT) was originally designed to ensure that everyone would pay his or her fair share of income taxes. In 1987, only 140,000 taxpayers were subject to the AMT. Since then, however, it has evolved into a separate tax regime that will affect millions of unsuspecting taxpayers at some time in the future.

The wisdom of conventional tax planning advice to defer income and accelerate certain types of deductions may not hold true if an individual expects to be subject to the AMT. Accordingly, during the year-end tax planning process, it is critical that you determine if you are subject to the AMT in both the current year and following year. This analysis is even more complicated this year—if not impossible—because the AMT exclusion level as of this writing has not yet been extended, and next year's exclusion level is, of course, also unknown.

If you are continuously subject to the AMT, avoid investing in private-activity (municipal) bonds. Income from these bonds is taxable for AMT purposes. Furthermore, you should be aware that unusual combinations of income and deductions might require AMT planning that runs contrary to conventional tax-planning advice.

Although the exercise of an incentive stock option (ISO) does not give rise to regular taxable income to the employee, the difference between the exercise price and the market price of the stock must be recognized for AMT purposes for the year in which the option is exercised. Accordingly, the exercise of ISOs with a large bargain element often causes a tax liability under the AMT tax regime.

The AMT area is extremely complex, so generalizations are difficult. If you think you may be subject to the AMT, you should consult with your tax advisor before year-end to determine how to minimize your exposure.

Year-End Estate and Gift Tax Planning

Year-end planning from an estate planning perspective typically involves ensuring that "annual exclusion" gifts are completed by the end of the calendar year.

Under the federal gift tax system, each donor is permitted to make non-taxable gifts of a certain amount each year to any donee. These gifts are called "annual exclusion" gifts and do not count against the donor's lifetime gifts exemption (currently $1 million). In 2007, the annual gift exclusion level increased to $12,000 and it will remain at that level in 2008. To the extent not used, the annual exclusion evaporates at the end of each calendar year.

Annual transfers that take advantage of this exclusion can both diminish the donor's estate tax liability and improve the lives of the recipients. These gifts can take many forms (cash, stocks, real estate, partnership interests) and can be given outright through Uniform Transfers to Minors accounts, and even through a trust—provided it contains special provisions designed to allow the gift to qualify for the annual exclusion.

Personal Investments 2007

Dividends & Interest

Interest

Taxable interest will be reported to you by the payer on Form 1099-INT or Form 1099-OID (for the annual taxable portion of the imputed interest on original issue discount bonds).

Tax-exempt interest will be reported to you by the state or local government payer on Form 1099-INT. In addition, typically mutual funds that hold tax-exempt bonds will report this information to you on the 1099-DIV form. You must report the amount of tax-exempt interest you receive on Schedule B of Form 1040. Although you do not have to pay ordinary income tax on it, the amount of tax-exempt interest you receive can affect your tax status in some situations, including your exposure to the alternative minimum tax.

You should not report interest earned on your IRA or Coverdell education savings accounts, since these are exempt from tax.

Dividends

Dividends you receive from stocks you hold will be reported to you on IRS Form 1099-DIV. Box 1a on the form will report total ordinary dividends you have received.

Qualified dividends are eligible for a lower tax rate than other ordinary income. Dividends that qualify for this treatment will be reported in box 1b of your Form 1099-DIV.

Some dividends are not qualified for the reduced rates. Generally, these include:

- Dividends on stock that you held for less than 61 days during the 121-day period that began 60 days before the ex-dividend date,
- Dividends related to short sales,
- Dividends received from tax-exempt organizations under sections 501 and 521,
- Dividends from a mutual savings bank for which the bank took a deduction, and
- Deductible dividends paid on employer securities.

Dividends from mutual funds will qualify for reduced rates to the extent that they are from qualified dividends from stocks held by the fund.

In general, dividends from REITs will not qualify for the reduced rates. Typically, dividends paid by REITs are comprised of rents and other earnings, and not dividends from other corporations. Therefore, the majority of the dividends paid by REITs will be taxed as ordinary income and only a small portion may qualify as dividend income.

[You will receive a 1099-DIV from any mutual fund you hold; for more information on taxes and mutual fund dividends and distributions, see the section starting on page 17.]

Holding Period

One of the requirements for dividends to qualify for the 15% maximum tax rate is that you must have held the dividend-paying stock for more than 60 of the 121 days surrounding the "ex-dividend" date of the stock.

The 121-day period begins 60 days prior to the ex-dividend date and ends 60 days after the ex-dividend date. When counting the number of days you have held the stock, you include the day you disposed of the stock, but not the day you acquired it. If the stock fails to meet the holding period requirement, the dividend will not be eligible for the 15% tax rate and, consequently, the dividend will be taxed at ordinary income tax rates.

Margin Accounts

'Disqualified' Dividends

Be aware of a twist to the holding period requirement if you receive dividends on stock held in a margin account — not all of your dividends may qualify for the 15% tax rate.

Generally, when you enter into a margin agreement with a broker, the agreement contains a clause that allows the broker to borrow shares from your account and return them at a later date, without your pre-approval. Typically, the broker will borrow shares from a large pool of shares it holds in street name on behalf of all its customers and lend the shares to another party to use in a short sale. The broker will later allocate the borrowed shares to particular customers. The loan of the shares will affect your holding period of the dividend-paying stock, which could potentially make the dividends ineligible as qualified dividend income.

This occurs because you no longer own the shares if the broker borrows them. Instead of receiving dividends, you will receive "payments in lieu of dividends," which are not dividends and are not eligible for qualified dividend income treatment. Payments in lieu of dividends are taxed at ordinary income tax rates.

Prior to 2003, dividends and payments in lieu of dividends were typically both reported on Form 1099-DIV. Currently, however, brokers are required to report payments in lieu of dividends on Form 1099-MISC, as opposed to Form 1099-DIV. For tax planning purposes, you may want to consider moving your high-dividend-paying stocks from margin accounts to cash accounts, in order to increase the likelihood that the dividends qualify for the 15% tax rate. Alternatively, you could inquire as to whether the broker has historically borrowed shares from your account. If so, you should require the broker to sign an agreement against borrowing stock from your account. Some brokerage firms have policies that state that they generally do not borrow shares from non-institutional investors.

Taxwise

Dividends on insurance policies are a partial return of premiums paid and do not need to be reported, unless they exceed the total of all net premiums you paid for the contract. Taxable dividend distributions from life insurance companies are reported on form 1099-R.

Taxwise

Although you are allowed to deduct investment interest expense on Schedule A of Form 1040, it is limited to the amount of current year net investment income (generally interest, dividends, annuities and royalties). Dividends subject to the lower tax rate are not treated as investment income for purposes of deducting investment interest expense. However, you may elect to tax dividends and long-term capital gains at ordinary tax rates to qualify that income for calculating the interest expense deduction.

Gains & Losses

A "capital gain" is the profit you make when you sell a capital asset. Almost everything you own, including your investments, is a capital asset. Stocks, bonds, mutual fund investments, gold, silver, antiques, personal residences, gemstones and oriental rugs all fall into the capital assets category.

A long-term capital gain is the profit you make when you sell a capital asset that you have held for more than a year. A short-term capital gain, on the other hand, is the profit you make when you sell a capital asset that you have held for a year or less.

Capital Gains Rates

Long-term capital gains are now taxed at rates that are more favorable than those that apply to ordinary income, such as salaries and interest.

Long-term capital gains are taxed at the maximum long-term capital gains rate of 15%; for taxpayers whose top bracket is 15%, the long-term capital gains rate is an even lower 5%. Short-term capital gains are taxed at the same rate as ordinary income.

For your investments inside a qualified pension or profit-sharing plan, capital gains rules do not apply. On the plus side, the investment return on plan assets is not subject to taxes as long as the dollars remain inside the plan. On the negative side, dollars withdrawn from a plan are subject to ordinary income tax rates, so capital gain income inside a plan becomes ordinary income upon distribution.

Other Special Rates

Section 1250 Property

The lower capital gains rates do not apply in all situations. The long-term capital gains rate on business or investment real estate (called "section 1250 property" on the tax forms) will be 25% up to the amount of depreciation on the property while you owned it. However, there are no losses counted in the 25% rate group and any loss from this group must be taken into account in computing net gain or loss in the 15% rate group.

Collectibles

Also, the long-term capital gains rate on collectibles such as art, rugs, jewelry, precious metals or gemstones, stamps or coins, fine wines, or antiques remains at 28%.

Holding Period

A capital gain becomes long term if it is held for more than 12 months. The holding period begins the day after purchase and ends the day of sale (trade dates, not settlement dates).

Your brokerage firm will send you a Form 1099-B list-

YOUR CHILD'S INVESTMENT INCOME: THE "KIDDIE" AGE INCREASES

The kiddie tax rules require that part or all of a child's investment income be taxed at the parents' income tax rate, which is typically higher than the child's rate. The rules were put in place to limit the tax benefit families had been receiving by shifting income to children, who would then be taxed at lower rates applicable to individuals with little income.

Originally, the kiddie tax applied to children under the age of 14, which is how it became known as the "kiddie" tax. But the age limit keeps increasing. In 2006, the age limit was raised to age 18. This year, Congress extended it even further, and starting in 2008 it may apply to "children" up to age 24, depending on the extent to which you are supporting them and whether they are still in college.

For 2007, the kiddie tax rule applies if the child is 17 or under by the end of the year, and the child's total investment income for the year was more than $1,700. Investment income includes interest, dividends, capital gains and other unearned income. That means that, for 2007, a child 18 or older can still get the full benefit of lower tax rates. Next year, however, the rules become more complex for children 18 through 23.

Starting in 2008, the new rules extend the kiddie tax to older children, depending on how much earned income they have and whether or not they are full-time students:

- *Starting in the year that your child turns 18, the kiddie tax applies if your child's earned income (including salaries and wages, commissions, professional fees and tips) is less than half of the child's overall support.*
- *Starting in the year your child turns 19, the kiddie tax applies if your child is a full-time student.*
- *The kiddie tax ceases to apply starting in the year your child turns 24.*
- *The kiddie tax also does not apply if your child is married filing jointly.*

If you are subject to the kiddie tax rules, it can be reported in two ways:

- *Your child's investment income can be reported on Form 8615, which should be attached to the child's federal income tax return, or*
- *You can choose to report your child's investment income on your own tax return if the child's income consists entirely of interest and dividends (including capital gain distributions) and the amount received is less than $8,500 in 2007. If you choose this option, fill out Form 8814, Parent's Election to Report Child's Interest and Dividends, and include it with your own tax return. Be aware, however, that this option may reduce certain credits or deductions that parents may claim.*

Although the kiddie tax is calculated based on the parents' tax rate, it is owed by the child. Wages and other earned income received by a child of any age is taxed at the child's tax rate. More information can be found in IRS Publication 929, Tax Rules for Children and Dependents.

ing the proceeds from all your sales for the year based on the trade date. It is best to rely on this document for information when tax filing time rolls around, rather than on your periodic brokerage statements.

Why not use your brokerage statement? If you buy or sell stock near the end of the year, these trades may not appear on your December statement, and, as a result, you may overlook them. But you should reconcile the information in your records with what is reported on your Form 1099-B.

If your Form 1099-B is incorrect, contact your brokerage firm or other financial services institution, and ask them to issue a corrected form. It is important that amounts shown on Form 1099-B be included in the proceeds reported on your Schedule D, "Capital Gains and Losses," of Form 1040. If they do not match, the IRS will likely send you a notice and may assess a penalty for negligence if you have failed to report income.

Calculating Your Gain

To determine a gain or loss on the sale or exchange of an asset, an asset's "basis" is subtracted from the sales proceeds. Basis is generally the amount you pay for an asset plus certain expenses such as sales commissions.

For each investment sold or exchanged during the year, you must know the:

- number of shares bought,
- amount paid per share,
- date of each purchase,
- total dollar amount of the purchase, including items such as commissions and fees,
- number of shares sold or exchanged,
- price received per share from the sale or exchange,
- date of each sale or exchange, and
- the total dollar amount received from each sale or exchange.

This information may be obtained from personal records, monthly statements and Form 1099-Bs from brokerage firms or financial institutions. If less than all of the investment in a particular stock, bond, or other security is sold, you must also identify which shares were sold so you can determine the proper basis to use. There are two different methods to identify the shares sold.

Selling Specific Shares

If you know how many shares you bought when you purchased them and how much you paid, the law requires you to use the specific-share method. This method may give you a choice about whether to realize a gain or a loss.

Example: You own 565 shares of stock in XYZ Corp. You purchased 250 shares at $10/share in February 200A, 15 shares at $15/share in January 200B, 200 shares at $14/share in July 200B, and 100 shares at $12/share in August 200B. Assume your broker holds your shares for you. Now, you inform your broker, in writing, on June 1, 200C, to sell the 200 shares you purchased in July 200B at $14/share. Because you specified the shares to sell, figuring your basis is easy. In this case, it is $14/share—the price you paid for them.

If you sell the 200 shares at $11/share, you report a short-term capital loss of $3/share—that is, your $11 selling price less your $14 basis. Your total loss comes to $600 ($3 × 200 shares). Since you owned the shares less than a year, your loss is a short-term one.

You may use your $600 loss to offset some capital gains you may have had from other transactions. If you had no capital gains, the rules say you can subtract the $600 from your ordinary income. However, there is a limit on how much capital loss you may deduct each year from your ordinary income.

Taxwise

It is important that you have a record of your instructions to sell specific shares, so be sure to keep a copy of the dated letter sent to your broker or fund. Also, you should receive written documentation back from your broker confirming that specific shares were sold. Such instructions are only effective if the stock is held in "street name" – that is, the stock is held for you in the name of the broker or fund. If the shares sold are held in your name, it does not matter what the instructions were – the actual certificates delivered are the ones that are considered sold.

First In, First Out

Where there are no records concerning the purchase of a stock, bond, or other investment, you may have to use the first in, first out (FIFO) method (in other words, the first bought is the first one sold). Also, if you do not specify which shares are to be sold in advance, you will be required to use the FIFO method.

Exceptions

There are a few exceptions to the rules governing basis:

- ***Gifts:*** If you receive stock as a gift, your basis is the basis of the stock to the donor at the time of the gift. In other words, the donor's basis becomes your basis. What if you sell the stock at a loss? Then your basis is the lesser of the donor's basis or the fair market value of the stock on the date the gift was made.
- ***Wash sales:*** A wash sale is a sale of stock, including stock in a mutual fund, at a loss either 30 days before or after you make another purchase of the same (or substantially identical) stock. (For more on this, see page 16.) A wash sale that results in a loss may not be deducted. Your basis in the new stock is what you paid for it, but it is increased for any loss that is disallowed.
- ***OIDs:*** With original issue discount securities, your basis is the amount you paid for the securities plus the interest income that accrues annually.
- ***Amortized bond premiums:*** If you deducted the amortization of bond premiums, the deductions will reduce your basis in the bond.
- ***Inheritances:*** If you inherit stock or some other capital asset, your basis is either the fair market value of the asset on the day the person died or its value on the alternative valuation date if the executor of the estate chooses a different date to value the estate. Generally, you should use the value shown on the estate tax return.
- ***Stock dividends, splits, and reorganizations:*** Your stock basis can be affected if the corporation issues stock dividends, declares a stock split, or undergoes a reorganization. These events are generally non-taxable at the time they occur. Typically, your original basis will be allocated equally among shares owned after the event. [For more on this, see the box below.]
- ***Mutual funds:*** See the Mutual Fund section beginning on page 17 for information concerning the calculation of the capital gain or loss.

Splits, Dividends, & Mergers

One day when you're reviewing your brokerage account statement, you might find that you have more or less shares of a particular stock than you recall from the previous month's statement. You might even find yourself owning shares of a company you know you never purchased. If so, it is likely that your company has undergone a stock split, reverse split, stock dividend, or merger. Be aware that such events will alter your basis per share and, as a result, the capital gain or loss you recognize should you subsequently sell less than 100% of your holdings in that stock.

In the case of a stock split, you end up with more shares than you previously had, but no change to your total basis occurs.

However, the per-share basis value will change. For example, if you purchased 100 shares of a stock for $5 per share, your basis is $500. If the stock splits 2-for-1, you will now have two shares for each one share you previously held, thus doubling your shares to 200. Your total basis remains at $500, but your basis per share is now $2.50 ($500 divided by 200 shares). When you sell the shares, $2.50 is the per-share basis amount you should use to calculate your capital gain or loss. The acquisition date for the new 100 shares is the same as for the original 100 shares.

A reverse split is the opposite of a normal split in that it results in fewer shares being held. In our previous example, if the 100 shares you own split 1-for-2, you will have one share for every two shares you previously held, thus halving your shares to 50. Again, your total basis remains at $500, but your basis per share is now $10 ($500 divided by 50 shares).

A stock dividend is a dividend paid in stock instead of cash. Its effect on basis is similar to that of a stock split. For example, assume you purchased 100 shares of a stock for $5 each, so that your total basis is $500. If a company declares a stock dividend of 10%, you will receive additional shares equal to 10% of the number of shares you already own. In this case, you will receive 10 additional shares (100 shares multiplied by 10%). Your total basis remains at $500, but your basis per share is now $4.55 ($500 divided by 110 shares).

Finally, when two companies merge, you may wind up owning an entirely new stock. For example, assume you owned 100 shares of Company X with a basis of $500 before the merger. The merger requires you to exchange your Company X shares for Company Y shares. After the merger, you now own 75.4 shares of Company Y. Your total basis remains at $500, but your per-share basis has changed. Before the merger it was $5 per share ($500 divided by 100 shares); after the merger it has become $6.63 per share ($500 divided by 75.4 shares).

You should note that with mergers, the new company may decide to cash you out of any partial shares you own after the merger. You might receive a payment to compensate you for the sale of your partial shares. In our example, Company Y may decide to pay you for the 0.4 share. In this case, your basis of the 0.4 share sold would be $2.65 (0.4 shares multiplied by $6.63 per share). In this case, your taxable gain is the difference between the amount you were paid for the fractional share and $2.65. Your remaining shares continue to have a basis of $6.63 per share for a total basis in your holdings of $497.25.

Capital Losses

Capital losses first reduce capital gains. Long-term losses reduce long-term gains first, and short-term losses reduce short-term gains first. Any long-term losses left over reduce short-term gains and vice versa.

If you still have losses remaining after offsetting capital gains, you can reduce your "ordinary" income by up to $3,000. Losses not used this year can be carried forward to future years until they are used up.

Worthless Securities

A capital loss can be claimed in the year securities (e.g., stock, bonds, etc.) become worthless. Determinations of whether stock has become worthless and, if worthless, the year in which it ceased to have value, are questions of fact, and the burden of proof is on the taxpayer. Thus, you should consult your tax advisor before claiming a deduction on worthless securities.

Taxwise

Caution: Mere shrinkage in value of stock of a corporation through market fluctuations or otherwise does not entitle you to a loss deduction, and, in such a case, the loss is allowable only upon the disposition of the stock.

Capital Losses on Collectibles

If you invest in jewelry, coins, stamps, antiques or the like, and you incur capital losses on the sale of these items, the tax law allows a deduction only if the following conditions are met:

- You must prove that your primary purpose in purchasing the item was to make a profit; and
- You must show that you did not purchase these items purely as a hobby or for your personal enjoyment.

Taxwise

Tip: Maintain detailed records on the purchase and sale of collectibles. Your reputation as an investor is your best defense in the event of an IRS audit.

Wash Sales

If you sell an investment at a loss and then acquire, or enter into a contract or option to acquire, substantially identical stock or other securities during the period which begins 30 days before the date of sale and ends 30 days after the date of sale, the loss on the sale of those stocks or securities will be disallowed. This unrecognized loss is added to the basis of the new securities acquired. In other words, if you sell a stock or bond to recognize the tax loss, you must not buy it back for at least 31 days before or after the sale date.

It is important to point out that this rule only applies to losses; gains are taxable in the year of the sale. Also, these rules do not apply to commodity futures and foreign currencies, but they do apply to stock options (puts and calls).

Many have tried to avoid the wash sale rules by having a related party purchase the substantially identical securities after the sale. Examples of related-party transactions include an exchange between family members (including

parents, grandparents, siblings, children, and grandchildren and excluding in-laws, stepparents, stepchildren, aunts, uncles, nieces, nephews, and cousins) or an exchange between an individual and a corporation where the individual owns at least 50% of the corporation. Other examples of related-party transactions are an exchange between a grantor and fiduciary of a trust, as well as an exchange between the fiduciary and beneficiary of the trust. In these situations, the loss is not allowed.

Keep several important points in mind if you have losses you would like to recognize:

- You can sell stock in one company and buy stock in a similar but different company, without invoking wash-loss rules. However, a different class of stock in the same company will create a wash-loss event.
- A bond will be considered similar enough to another bond to invoke these rules if attributes such as maturity, investment grade, and yield to maturity are similar enough to constitute a substantially equivalent security to the one sold—i.e., the issuer does not have to be the same to cause these rules to apply. This is generally determined on a facts-and-circumstances basis, and expert advice may be required.
- Mutual funds are considered separate and distinct. Therefore, even if two funds hold substantially identical securities, moving assets from one fund to another will allow for recognition of any loss realized on the sale.

Mutual Funds & Taxes

If you are a mutual fund shareholder, you will receive tax reporting statements with information on each individual fund by late January. These statements include information that the fund reports to the IRS on Forms 1099-DIV (which reports fund distributions to shareholders) and 1099-B (which reports sales of fund shares). You report this information to the IRS on your income tax return, Form 1040—with each fund reported separately, even if it is within the same mutual fund family.

Mutual Fund Distributions

Investment returns generated by a mutual fund can be in the form of dividends, interest, and/or capital gains and losses. A mutual fund is required to distribute dividends, interest and net realized gains to you each year.

Mutual fund distributions are taxable whether you take them in cash or reinvest them in fund shares. There are two exceptions:

- Income dividends from municipal bond funds are usually exempt from state and local taxation, depending on what portion of the fund's assets were invested in a particular state; and
- Income dividends and net capital gains distributed to IRA and other retirement accounts are tax-sheltered until withdrawn.

Distributions are taxable for the year in which they are paid. However, the tax law states that mutual fund dividend or capital gains distributions declared within the last three months of the year but paid the following January are taxable as though they were paid on December 31. Therefore, such distributions are included on Form 1099-DIV.

The status of any capital gains or dividend distributed to you by a mutual fund depends on how long the fund owned the securities that produced the gain or dividend—not on how long you owned shares in the fund. The information you will need to determine how your distributions are taxed will be on your fund's Form 1099-DIV. This year's Form 1099-DIV includes the following distribution information:

- Total ordinary taxable dividends, and the portion that qualifies for the lower dividend rates;
- Total long-term capital gains distributions and the amount of the distribution that is subject to special other gains rates, such as section 1250 and collectibles gain;
- Non-taxable distributions, which are non-taxable because it is a return of your cost;
- Any federal income taxes withheld;
- Your share of investment expenses of a non-publicly offered mutual fund; and
- Foreign taxes paid (and which you may be able to claim as a deduction or credit).

What about losses?

A mutual fund's capital losses are never distributed to shareholders, but are used to offset capital gains realized by the fund during the year. Any additional losses are carried forward by the fund to apply against gains realized in the future. The only losses you can claim are those you may have incurred when you redeemed your own shares of a fund.

Save Money

Because distributions are taxed even if they are reinvested, it is important to remember that you should add reinvested income dividends and capital gains (from both taxable and tax-free funds) to your original cost basis when it comes time to figure gains or losses on any mutual fund shares sold. If you do not, you will, in effect, be paying taxes twice on those distributions.

Taxwise

When a distribution is made, the net asset value (NAV) of the fund decreases by an equal amount. Suppose the NAV of your fund XYZ is $20 per share on December 20. On December 21, the fund makes a distribution of $2 per share, and as a result, the NAV decreases by a like amount to $18 per share. Since you received the $2, you still have $20 of asset value, but now $2 is subject to tax. The $2 is taxable even if you reinvest it in that fund, although the reinvested amount increases your tax basis in the fund.

Mutual funds commonly make distributions toward the end of the year. Investors must be wary of this distribution date. Generally, you should not invest in a mutual fund shortly before its distribution date, because a portion of your investment will be immediately returned to you with an accompanying tax liability.

Most mutual funds should be able to give you a good idea of when their year-end distributions will take place, so calling the fund company prior to investing can be a wise move.

Selling Mutual Fund Shares

Shareholders can generate capital gains by selling or exchanging shares in mutual funds (except money market funds, which are managed to maintain a stable share price).

The tax rate that applies to your sale of mutual fund shares depends on how long you held the shares. Short-term capital gains for securities held one year or less are taxed at ordinary income rates. Long-term gains on securities held more than one year receive the more favorable rates.

There are two methods of computing the basis on mutual fund shares. The first is the cost method, which includes the option to use either specific-share identification or the first-in, first-out (FIFO) convention. The second is the average-basis method, which includes computing the basis under either the single- or double-category method.

Cost Method

Specific-share identification: Under this method, you are able to choose the shares you want sold. The downside to this method is that you are required to keep very detailed records. The IRS also requires you to inform the broker at the time of the sale which shares are being sold. The broker is required to provide a written confirmation to the IRS of your request.

This method is recommended to those who want to match capital losses with capital gains. This method offers the flexibility needed to effectively implement a "matching strategy."

First-in, first-out (FIFO): This method is somewhat less time-consuming than specific-share identification. Tracking the basis of all shares acquired is still required, but identifying shares sold is easier. Under this method, the basis of shares sold is assumed to be the basis of the first shares acquired. Also, there are no special IRS reporting requirements.

During a rising market, this method will produce a higher income tax liability for you. Over the long term, however, the tax consequences arising from using the average-basis method or the first-in, first-out method will be comparable.

Average-Basis Method

Single Category: Under this method, the basis of the shares sold is determined by computing the average cost of all the shares owned. This is done by calculating the total cost of the shares owned and then dividing this figure by the total number of shares owned. The holding period is determined using the FIFO method. If additional shares are acquired after a sale transaction, the average basis must be recalculated. Reinvested dividend and capital gain distributions will require ongoing recalculation of basis.

Double Category: The basis of the shares is computed in the same way as for the single-category method, with the exception that the shares held for less than a year are separate from the shares held for more than a year. You choose the category from which the shares are to be sold to determine whether the gain or loss will be short term or long term. Also, it is necessary for the broker to provide a written confirmation to the IRS specifying which category you chose.

If you hold mutual funds, it is also important to understand that the wash-sale rules do apply when dealing with funds as well as stocks and bonds (see page 16 for an explanation).

Taxwise

Unless you are conducting transactions in a tax-sheltered retirement plan, an exchange of assets from one fund to another is the same as a sale and purchase for tax purposes. In January, each mutual fund reports proceeds of sales (redemptions or exchanges) made during the year to the IRS and to you on Form 1099-B. The 1099-B does not need to be attached to your Form 1040, but the data on it should match what you report on Schedule D of Form 1040.

Taxwise

There is a special rule that applies if you have sold mutual fund shares held for six months or less at a loss. If you have received a capital gain distribution, a long-term capital loss must be recognized to the extent of the distribution. Any loss in excess of the distribution

is treated as a short-term loss. This has the effect of offsetting the capital gain tax benefit of the distribution against the loss realized on sale.

A similar rule applies to tax-exempt interest received on mutual fund shares that have been held for six months or less and sold at a loss. A loss is disallowed to the extent of tax-exempt interest received. Any loss in excess of the tax-exempt interest is considered short-term capital loss.

WHAT YOU CAN KEEP FROM SELLING YOUR HOME

You may be able to exclude up to $250,000 of gain ($500,000 for married taxpayers filing jointly) when you sell your main home. The exclusion is allowed each time you sell your main home, but no more than once every two years.

To exclude the gain, you must have owned the home and used it as your principal residence for at least two out of the five years before its sale. Periods of use include short absences (such as summer vacations), but longer breaks (such as one-year sabbaticals) do not. You also must not have excluded the gain on another home sale during the two years before the current sale.

Married taxpayers filing a joint return can exclude gains if either qualify for the year of the sale, but both spouses must meet the use test to claim the $500,000 maximum exclusion.

If you do not meet the ownership and use tests, you may be allowed to exclude a reduced amount if the sale was due to health, a change in employment or certain unforeseen circumstances.

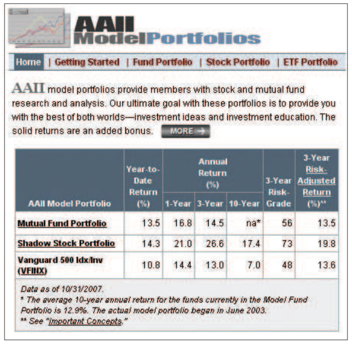
Excluded gains are not reported on your federal tax report; unexcluded gains are reported on Schedule D, Capital Gains or Losses.

For a complete description of the rules, see IRS Publication 523, Selling Your Home.

AAII MODEL PORTFOLIOS

AAII.com's Model Portfolios area provides specific guidance for developing an effective investment program. Although not intended as a complete advisory service, the portfolio collection offers an ongoing stream of stock and mutual fund research, ideas and analysis.

Each approach that we present shares the same philosophy: an emphasis on consistency, risk control, and selections that are ideal for individual investors, not institutions. AAII Model Portfolios can be found at www.aaii.com/aaiiportfolios, or by simply clicking on the Intro to Portfolios link in the AAII.com navigation bar.



AAII ModelPortfolios

Home | Getting Started | Fund Portfolio | Stock Portfolio | ETF Portfolio

AAII model portfolios provide members with stock and mutual fund research and analysis. Our ultimate goal with these portfolios is to provide you with the best of both worlds—investment ideas and investment education. The solid returns are an added bonus. MORE

AAII Model Portfolio	Year-to-Date Return (%)	Annual Return (%)			3-Year Risk-Grade	3-Year Risk-Adjusted Return (%)**
		1-Year	3-Year	10-Year		
Mutual Fund Portfolio	13.5	16.8	14.5	na*	56	13.5
Shadow Stock Portfolio	14.3	21.0	26.6	17.4	73	19.8
Vanguard 500 Idx/Inv (VFINX)	10.8	14.4	13.0	7.0	48	13.6

Data as of 10/31/2007.
** The average 10-year annual return for the funds currently in the Model Fund Portfolio is 12.9%. The actual model portfolio began in June 2003.*
*** See "Important Concepts."*

The Model Shadow Stock Portfolio

The Shadow Stock Portfolio provides guidance for investing in the promising micro-cap value sector of the market. Specific direction is provided as to how this model portfolio, and variations on it, fit into an investment program (***www.aaii.com/stockportfolio***).

The Model Mutual Fund Portfolio

The funds that we highlight in the Model Fund Portfolio must pass stringent requirements that include consistency, risk control, modest fees, and low turnover. AAII examines the different selection criteria on an ongoing basis, discussing variations that can affect risk (***www.aaii.com/fundportfolio***).

VISIT AAII'S MODEL PORTFOLIOS AREA TODAY!

Go to the AAII.com home page and click on Intro to Portfolios. To access members-only areas of the AAII Web site, simply type in your 10-digit AAII member number (from the mailing label on your *AAII Journal*) for both Login Name and Password when prompted.

2007 Tax Rates

INCOME TAX

For Single Taxpayers

Taxable Income Over ($)	Taxable Income But Not Over ($)	The Tax Is	Of the Amount Over
0	7,825	10%	$0
7,825	31,850	$782.50 + 15%	$7,825
31,850	77,100	$4,386.25 + 25%	$31,850
77,100	160,850	$15,698.75 + 28%	$77,100
160,850	349,700	$39,148.75 + 33%	$160,850
349,700	–	$101,469.25 + 35%	$349,700

For Married Taxpayers Filing Joint Returns

Taxable Income Over ($)	Taxable Income But Not Over ($)	The Tax Is	Of the Amount Over
0	15,650	10%	$0
15,650	63,700	$1,565.00 + 15%	$15,650
63,700	128,500	$8,772.50 + 25%	$63,700
128,500	195,850	$24,972.50 + 28%	$128,500
195,850	349,700	$43,830.50 + 33%	$195,850
349,700	–	$94,601.00 + 35%	$349,700

For Married Taxpayers Filing Separate Returns

Taxable Income Over ($)	Taxable Income But Not Over ($)	The Tax Is	Of the Amount Over
0	7,825	10%	$0
7,825	31,850	$782.50 + 15%	$7,825
31,850	64,250	$4,386.25 + 25%	$31,850
64,250	97,925	$12,486.25 + 28%	$64,250
97,925	174,850	$21,915.25 + 33%	$97,925
174,850	–	$47,300.50 + 35%	$174,850

For Individuals Filing as Head of Household

Taxable Income Over ($)	Taxable Income But Not Over ($)	The Tax Is	Of the Amount Over
0	11,200	10%	$0
11,200	42,650	$1,120.00 + 15%	$11,200
42,650	110,100	$5,837.50 + 25%	$42,650
110,100	178,350	$22,700.00 + 28%	$110,100
178,350	349,700	$41,810.00 + 33%	$178,350
349,700	–	$98,355.50 + 35%	$349,700

CAPITAL GAINS AND DIVIDENDS

	Taxpayers in 15% Bracket or Below (%)	Taxpayers Above the 15% Bracket (%)
Short-Term Capital Gains	taxed as income	taxed as income
Long-Term Capital Gains*	5	15
Qualified Dividends	5	15
Collectibles**	28 maximum	28 maximum
Real Estate Depreciation Recapture (Section 1250 Property)	25 maximum	25 maximum

** For investments held longer than one year.*

*** Includes art, rugs, jewelry, precious metals or gemstones, stamps or coins, fine wines and antiques.*

2007 Allowable Tax Benefits

STANDARD DEDUCTION

Under Age 65	
Married, Filing Joint	$10,700
Single	$ 5,350
Married, Filing Separate	$ 5,350
Head of Household	$ 7,850
Additional—Age 65 or Older	
Married	$ 1,050
Single	$ 1,300
Additional—Blind	
Married	$ 1,050
Single	$ 1,300

PERSONAL EXEMPTION

$3,400

MAXIMUM CHILD TAX CREDIT

$1,000 per child under 17 years

STANDARD MILEAGE DEDUCTIONS

Business Standard Mileage Rate	48.5 cents
Medical Standard Mileage Rate	20.0 cents
Moving Standard Mileage Rate	20.0 cents
Charitable Serv Standard Mile Rate	14.0 cents

DEDUCTIBLE IRA CONTRIBUTION

If taxpayer and spouse NOT covered by employer-sponsored plan

If younger than 50	$4,000
If 50 or older	$5,000

MAXIMUM 401(K) EMPLOYEE CONTRIBUTION

If younger than 50	$15,500
If 50 or older and plan allows catch-up contributions	$20,500

SELF-EMPLOYED MEDICAL INSURANCE PREMIUM DEDUCTION

100%

ANNUAL GIFT TAX EXCLUSION (PER PERSON)

$12,000

ESTATE TAX EXEMPTION

$2 million

2007 Other Tax Items

2007 SOCIAL SECURITY TAX RATES

	Employers & Employees	Self-Employed	Wage Limits
Social Security	6.20%	12.40%	$97,500
Medicare	1.45%	2.90%	no limit
Total	7.65%	15.30%	

2007 SAFE HARBOR FOR UNDERPAYMENT PENALTY

Avoid underpayment penalties by paying (through witholding or estimated tax payments):

AGI $150,000 or less ($75,000 married filing separate)
- 100% of prior tax liability or
- 90% of current year tax liability

AGI $150,000 or greater ($75,000 married filing separate)
- 90% of current year tax liability or
- 110% of prior year tax

2007 ITEMIZABLE DEDUCTIONS

Among other items they include:
- Interest and taxes on your home
- Uninsured medical expenses above 7.5% of AGI
- Miscellaneous itemized deductions above 2.0% of AGI
- Uninsured casualities or theft losses above 10.0% of AGI
- Contributions to qualified charities*
- You can choose to itemize state and local sales taxes instead of income taxes, but this option expires after 2007.

**New rules apply for certain charitable donations.*

2007 Tax Benefit Phase-Out Levels

PERSONAL EXEMPTION

	AGI Phase-Out Level
Married, Filing Joint	$234,600
Single	$156,400
Married, Filing Separate	$117,300
Head of Household	$195,500

In 2007, there is a 33.3% repeal of the personal exemption phase-out.

ITEMIZED DEDUCTION

	AGI Phase-Out Level
Married, Filing Joint	$156,400
Single	$156,400
Married, Filing Separate	$78,200
Head of Household	$156,400

In 2007, there is a 33.3% repeal of the itemized deduction phase-out.

IRA DEDUCTIBILITY

For those covered by employer pension plan [$4,000 maximum contribution per taxpayer; if 50 or older, maximum is $5,000]

	Modified AGI* Phase-Out Level
Married, Filing Joint	$83,000
Single	$52,000
Married, Filing Separate	$0
Head of Household	$52,000
Married, Filing Joint not covered by pension plan but spouse is	$156 ,000

ROTH IRA ELIGIBILITY

Maximum $4,000 non-deductible contribution; if 50 or older, maximum is $5,000

	Modified AGI* Phase-Out Level
Married, Filing Joint	$156,000
Single	$99,000
Married, Filing Separate	$0
Head of Household	$99,000

COVERDELL EDUCATION ACCOUNT

$2,000 maximum non-deductible contribution per beneficiary; withdrawals are tax-free for qualified education expenses

	Modified AGI* Phase-Out Levels
Married, Filing Joint	$190,000 to $220,000
Single	$95,000 to $110,000
Married, Filing Separate	$95,000 to $110,000
Head of Household	$95,000 to $110,000

**Modified AGI starts with your AGI (adjusted gross income) and adds back certain tax-exempt amounts including any IRA deductions.*

2007 Tax Forecasting Worksheet

This worksheet is designed for estimation purposes only and does not cover all the possible adjustments that may be required to arrive at actual taxable income (for example, Social Security benefits may be taxable in some circumstances) or to compute final income tax liability (for example, lump-sum distribution tax on retirement distributions). It should be adequate for most purposes and is a good starting point for discussions with your tax advisor, who can assist you in making exact calculations.

	2007	2008
Income		
1. Salaries per Form W-2	________	________
2. Non-qualified dividends and interest income	________	________
3. Net business income (losses)	________	________
4. Net capital gains and qualified dividend income[a]	________	________
5. Other gains (losses)	________	________
6. Passive income (losses) (subject to limitations)	________	________
7. Other income, including 85% of Social Security benefits, if applicable	________	________
8. Total income (sum of lines 1 – 7)	**$**________	**$** ________
Adjustments		
9. Alimony paid	________	________
10. Keogh contributions	________	________
11. Deductible IRA contributions	________	________
12. Moving expenses	________	________
13. Other ____________	________	________
14. Adjusted gross income (AGI) (subtract lines 9 – 13 from line 8)	$________	$ ________
Deductions		
15. Medical and dental expenses (excess over 7.5% of line 14) or self-employed health insurance	________	________
16. State and local income taxes	________	________
17. Real estate and property taxes	________	________
18. Home mortgage interest	________	________
19. Investment interest (limited to investment income)	________	________
20. Charitable contributions	________	________
21. Casualty or theft losses (excess over $100 plus 10% of line 14)	________	________
22. Miscellaneous expenses (excess over 2% of line 14)	________	________
23. Total deductions (sum of lines 15 – 22, less 3% of (line 14 – $156,400), or the standard deduction if greater)[b]	$________	$ ________
24. Personal exemptions ($3,400 each in 2007; $3,500 each in 2008)[b]	________	________
25. Regular taxable income (subtract lines 23 and 24 from line 14)	$________	$ ________
26. Regular tax (see tax rate tables)[a]	________	________
27. Tax credits	________	________
28. Regular tax (net) (subtract line 27 from line 26)	________	________
29. Alternative minimum tax[c]	________	________
30. Other taxes (self-employment tax, household help, and so forth)	________	________
31. Total tax (sum of lines 28, 29, and 30)	________	________
32. Total withholding and estimated tax payments	$________	$ ________
33. Balance due (refund) (subtract line 32 from line 31)	$________	$________

a. If your taxable income includes net capital gain and qualified dividend income, you may be eligible for a tax rate on that income that is lower than the tax rate that applies to your other income. Refer to IRS Form 1040, Schedule D.

b. In 2007, the phase-outs for itemized deductions and personal exemptions are reduced by 33.3%; in 2008, the phase-outs are reduced by 66.6%.

c. Use IRS Form 6251 as a worksheet and review the discussion on AMT on page 9.

2008 Tax Rates

INCOME TAX

For Single Taxpayers

Taxable Income Over ($)	But Not Over ($)	The Tax Is	Of the Amount Over
0	8,025	10%	$0
8,025	32,550	$802.50 + 15%	$8,025
32,550	78,850	$4,481.25 + 25%	$32,550
78,850	164,550	$16,056.25 + 28%	$78,850
164,550	357,700	$40,052.25 + 33%	$164,550
357,700	–	$103,791.75 + 35%	$357,700

For Married Taxpayers Filing Joint Returns

Taxable Income Over ($)	But Not Over ($)	The Tax Is	Of the Amount Over
0	16,050	10%	$0
16,050	65,100	$1,605.00 + 15%	$16,050
65,100	131,450	$8,962.50 + 25%	$65,100
131,450	200,300	$25,550.00 + 28%	$131,450
200,300	357,700	$44,828.00 + 33%	$200,300
357,700	–	$96,770.00 + 35%	$357,700

For Married Taxpayers Filing Separate Returns

Taxable Income Over ($)	But Not Over ($)	The Tax Is	Of the Amount Over
0	8,025	10%	$0
8,025	32,550	$802.50 + 15%	$8,025
32,550	65,725	$4,481.25 + 25%	$32,550
65,725	100,150	$12,775.00 + 28%	$65,725
100,150	178,850	$22,414.00 + 33%	$100,150
178,850	–	$48,385.00 + 35%	$178,850

For Individuals Filing as Head of Household

Taxable Income Over ($)	But Not Over ($)	The Tax Is	Of the Amount Over
0	11,450	10%	$0
11,450	43,650	$1,145.00 + 15%	$11,450
43,650	112,650	$5,975.00 + 25%	$43,650
112,650	182,400	$23,225.00 + 28%	$112,650
182,400	357,700	$42,755.00 + 33%	$182,400
357,700	–	$100,604.00 + 35%	$357,700

CAPITAL GAINS AND DIVIDENDS

	Taxpayers in 15% Bracket or Below (%)	Taxpayers Above the 15% Bracket (%)
Short-Term Capital Gains	taxed as income	taxed as income
Long-Term Capital Gains*	0	15
Qualified Dividends	0	15
Collectibles**	28 maximum	28 maximum
Real Estate Depreciation Recapture (Section 1250 Property)	25 maximum	25 maximum

** For investments held longer than one year.*
*** Includes art, rugs, jewelry, precious metals or gemstones, stamps or coins, fine wines and antiques.*

2008 Allowable Tax Benefits

STANDARD DEDUCTION

Under Age 65	
Married, Filing Joint	$10,900
Single	$ 5,450
Married, Filing Separate	$ 5,450
Head of Household	$ 8,000
Additional—Age 65 or Older	
Married	$ 1,050
Single	$ 1,350
Additional—Blind	
Married	$ 1,050
Single	$ 1,350

PERSONAL EXEMPTION

$3,500

MAXIMUM CHILD TAX CREDIT

$1,000 per child under 17 years

STANDARD MILEAGE DEDUCTIONS

Business Standard Mileage Rate	NA
Medical Standard Mileage Rate	NA
Moving Standard Mileage Rate	NA
Charitable Serv Standard Mile Rate	NA

NA: Not available. These rates have not yet been released by the IRS.

DEDUCTIBLE IRA CONTRIBUTION

If taxpayer and spouse NOT covered by employer-sponsored plan

If younger than 50	$5,000
If 50 or older	$6,000

MAXIMUM 401(K) EMPLOYEE CONTRIBUTION

If younger than 50	$15,500
If 50 or older	$20,500

SELF-EMPLOYED MEDICAL INSURANCE PREMIUM DEDUCTION

100%

ANNUAL GIFT TAX EXCLUSION (PER PERSON)

$12,000

ESTATE TAX EXEMPTION

$2 million

2008 Other Tax Items

2008 SOCIAL SECURITY TAX RATES

	Employers & Employees	Self-Employed	Wage Limits
Social Security	6.20%	12.40%	$102,000
Medicare	1.45%	2.90%	no limit
Total	7.65%	15.30%	

2008 SAFE HARBOR FOR UNDERPAYMENT PENALTY

Avoid underpayment penalties by paying (through witholding or estimated tax payments):

AGI $150,000 or less ($75,000 married filing separate)

- 100% of prior tax liability or
- 90% of current year tax liability

AGI $150,000 or greater ($75,000 married filing separate)

- 90% of current year tax liability or
- 110% of prior year tax

2008 ITEMIZABLE DEDUCTIONS

Among other items they include:

- Interest and taxes on your home
- Uninsured medical expenses above 7.5% of AGI
- Miscellaneous itemized deductions above 2.0% of AGI

**Note that new rules apply for certain donations.*

- Uninsured casualities or theft losses above 10.0% of AGI
- Contributions to qualified charities*
- You can itemize only state and local income taxes; sales taxes are not itemizable. However, Congress is considering legislation that may renew this option.

2008 Tax Benefit Phase-Out Levels

PERSONAL EXEMPTION

	AGI Phase-Out Level
Married, Filing Joint	$239,950
Single	$159,950
Married, Filing Separate	$119,975
Head of Household	$199,950

In 2008, there is a 66.6% repeal of the personal exemption phase-out.

ITEMIZED DEDUCTION

	AGI Phase-Out Level
Married, Filing Joint	$159,950
Single	$159,950
Married, Filing Separate	$79,975
Head of Household	$159,950

In 2008, there is a 66.6% repeal of the itemized deduction phase-out.

IRA DEDUCTIBILITY

For those covered by employer pension plan [$5,000 maximum contribution per taxpayer; if 50 or older, maximum is $6,000]

	Modified AGI* Phase-Out Level
Married, Filing Joint	$85,000
Single	$53,000
Married, Filing Separate	$0 to $10,000
Head of Household	$53,000
Married, Filing Joint not covered by pension plan but spouse is	$159,000

ROTH IRA ELIGIBILITY

Maximum $5,000 non-deductible contribution; if 50 or older, maximum is $6,000

	Modified AGI* Phase-Out Level
Married, Filing Joint	$159,000
Single	$101,000
Married, Filing Separate	$0
Head of Household	$101,000

COVERDELL EDUCATION ACCOUNT

$2,000 maximum non-deductible contribution per beneficiary; withdrawals are tax-free for qualified education expenses

	Modified AGI* Phase-Out Levels
Married, Filing Joint	190,000 to $220,000
Single	$95,000 to $110,000
Married, Filing Separate	$95,000 to $110,000
Head of Household	$95,000 to $110,000

Modified AGI starts with your AGI (adjusted gross income) and adds back certain tax-exempt amounts including any IRA deductions.

2008 Tax Planning Calendar

Tax and financial planning are activities best pursued year-round. Although the timing of some activities is critical, you should review all tax considerations from the perspective of your specific needs and establish an individualized planning calendar.

If the last day for filing a return, paying tax, or performing other activities falls on a Saturday, Sunday, or legal holiday (in the District of Columbia), you have until the next day that is not a Saturday, Sunday, or legal holiday to perform that act. Use the following list to remind yourself of important activities and dates:

First Quarter

General

- Complete Form W-4, Employee's Withholding Allowance Certificate, and adjust withholding, if needed.
- Evaluate before-tax and voluntary aftertax contributions to retirement plans.
- Apply for a Social Security number for any child who does not have one.

January 15

- Pay fourth-quarter 2007 estimated tax voucher if you did not pay your income tax for the year through withholding, or if you did not pay enough through withholding. You do not have to make this payment if you file your 2007 return and pay any tax due by January 31, 2008.
- Make quarterly defined-benefit Keogh contribution for preceding year.

January 31

- File your income tax return (Form 1040) for 2007 if you did not pay your last installment of estimated tax by January 15. Filing your return and paying any tax due by January 31 prevents any penalty for late payment of last installment.

Second Quarter

April 2

- Comply with minimum distribution rules for qualified plans if you attained age 70½ in the previous year.

April 15

- File individual and gift tax returns (or apply for an extension). If you want an automatic six-month extension of time to file the return, file Form 4868; or, you can get an extension (until October 15) by phone or over the Internet if you pay part or all of your estimate of income tax due with a credit card.
- File Schedule H (Form 1040) with your tax return if you paid cash wages of $1,500 or more in 2007 to a household employee.
- Report federal unemployment (FUTA) tax on Schedule H if you paid total cash wages of $1,000 or more in any calendar quarter of 2006 or 2007 to household employees.
- Pay first-quarter estimated tax if you are not paying your 2008 income tax through withholding or you will not pay enough that way.
- Make prior-year IRA and Coverdell Education Savings Account contributions.
- Make prior-year Keogh or SEP plan contribution (unless you applied for an extension of time to file your return).
- Make quarterly defined-benefit Keogh contribution for the current year.

June 16

- Pay second-quarter estimated tax voucher if you are not paying your income tax for the year through withholding, or if you are not withholding enough.

Third Quarter

July 15

- Make quarterly defined-benefit Keogh contribution for the current year.

September 15

- Pay third-quarter estimated tax voucher if you are not paying your income tax for the year through withholding, or if you are not withholding enough.

Fourth Quarter

General

Begin your year-end tax planning:

- Project your current year and next year tax liabilities.
- Evaluate the applicability of the AMT and other taxes.
- Adjust withholding, if necessary.
- Evaluate year-end capital transactions.
- Establish a separate Keogh plan for self-employment income.
- Comply with minimum distribution rules for qualified plans.

October 15

- If you extended your individual tax return, file your 2007 income tax return and pay any tax, interest and penalties due.
- Make quarterly defined-benefit Keogh contribution for the current year.

Throughout the Year

- Re-evaluate your long-term strategies.
- Evaluate your tax and financial strategy for receiving discretionary and mandatory retirement plan distributions.
- Rebalance investment portfolio and re-evaluate your uses of debt.
- Consider making gifts up to the annual gift tax exclusion.
- Evaluate passive loss exposure and potential investment shifts.
- If you have excess cash flow, consider how to invest those funds.
- Optimize mix of interest expense items.
- Consider making charitable contributions of property.
- Consider ways to fund your children's education.
- Evaluate your mix of portfolio and passive income.

2008 FEDERAL LEGAL HOLIDAYS

January 1—New Year's Day
January 21—Birthday of Martin Luther King Jr.
February 18—Washington's Birthday
May 26—Memorial Day
July 4—Independence Day
September 1—Labor Day
October 13—Columbus Day
November 11—Veterans Day Observed
November 27—Thanksgiving Day
December 25—Christmas Day